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4 June 1985

MEMORANDUM FOR: Ambassador Robert Morris

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SUBJECT: International Services in the Indian Economy [redacted]

1. On May 30, 1985, David Sloan requested background information on the services sector of the Indian economy for possible use by Under Secretary Wallis in his discussions with Indian Finance Minister Singh. [redacted]

2. Exports of labor and non-factor services make a major contribution to India's foreign exchange position. Tourist receipts, and remittances from Indian workers in the Middle East--which are probably the major component of private transfers--are especially important. Annex 1 provides selected balance-of-payments data for India. [redacted]

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3. Official Indian interest in expanding exports of services probably centers on three categories:

-- Computer software. (See Annex 2.)

-- Tourism, which Prime Minister Gandhi hopes to encourage.

-- Consultancy services. The Indian press reports foreign exchange receipts of \$64 million from consultancy services in the fiscal year that ended March 31, 1983. This probably does not include receipts from services that are an integral part of turnkey projects and support Indian exports of equipment and the supply of Indian labor. Most project and consultancy earnings come from the Middle East, Africa and Southeast Asia. [redacted]

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4. Almost all banking and insurance activity in India--except for the 132 branches of foreign banks--is nationalized. It accounts for about 3.6 percent of gross national product. In November 1983, there were 139 branches of Indian banks in other countries, but we believe they are active primarily in serving nonresident Indians and financing Indian trade and projects. Recent losses by Indian banks in the United Kingdom--a consequence of the bankruptcy of a nonresident Indian--may make Indian officials especially leery of discussing potential earnings from Indian banking services in other countries. [redacted]

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State Dept. review completed

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SUBJECT: International Services in the Indian Economy. [REDACTED]

5. Background information on recent changes in Indian economic policies and on India's international financial position is provided in Annexes 3 and

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6. Please do not hesitate to let us know if we can provide further information. Questions may be addressed either to me or Ange Hassinger, [REDACTED]

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[REDACTED]
Chief, Subcontinent Branch
South Asia Division/NESA

ANNEXES

As stated

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SUBJECT: International Services in the Indian Economy [REDACTED]

Distribution:

Original & 1 - Ambassador Robert Morris/Department of State
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INDIA: SELECTED BALANCE-OF-PAYMENTS DATA
MILLION \$

		1979/80	1980/81	1981/82	1982/83	1983/84	1984/85
Private Transfers:	Net	+ 1813	+ 2683	+ 2314	+ 2510	+ 2800	+ 2400
	Receipts	1823	2698	2333	2525	na	na
	Payments	10	15	19	15	na	na
Non-Factor Services:							
Foreign Travel:	Net	+ 1029	+ 1363	+ 1029	+ 982	+ 1165	+ 1020
	Receipts	1138	1477	1190	1174	1395	1220
	Payments	109	114	161	192	230	200
Transportation: ^a	Net	+ 81	8	- 95	302	291	- 300
	Receipts	394	458	445	423	422	na
	Payments	313	450	540	725	713	na
Insurance:	Net	+ 18	+ 18	+ 16	- 11	+ 11	na
	Receipts	53	61	61	60	60	na
	Payments	35	43	45	71	49	na
Government: ^b	Net	- 82	- 82	+ 18	- 22	+ 19	na
	Receipts	26	42	84	44	49	na
	Payments	108	60	66	66	30	na
Miscellaneous:	Net	- 4	- 8	+ 33	+ 290	+ 316	na
	Receipts	692	841	916	1119	1149	na
	Payments	696	849	883	829	833	na
Memorandum Item:							
	Receipts from non-factor services and private transfers as percent of merchandise exports.	54%	67%	58%	57%	57%	na

Fiscal years beginning April 1.

a Excluding freight and insurance on imports recorded on c.i.f. basis.

b Not included elsewhere.

All data are preliminary or estimates by World Bank, IMF, US Embassy and Agency.

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Indian Software Developments

Software development is expected to play a major role in Prime Minister Gandhi's campaign to expand India's technological capabilities, improve government efficiency and industrial productivity, and boost exports. The development of software for export is receiving particular emphasis. [REDACTED]

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Growing world demand has led to a shortage of qualified software engineers, [REDACTED] India is the most promising untapped source of such expertise. With an abundance of trained, English-speaking software engineers and low labor costs, India has the potential to become a major player in software production. New Delhi intends to exploit this capability. [REDACTED]

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Approximately 50 Indian firms are involved in software adaptation and development both for domestic use and for export. Applications include graphics software for the layout of printed circuit boards and engineering designs; systems for running computer numerically controlled (CNC) machines; engineering design software for process industries; accounting, inventory, and payroll applications; and software for process control, data logging and remote operation. [REDACTED]

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[REDACTED] Indian software engineers are also writing high-quality computer-aided design (CAD) software. [REDACTED]

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India has had a program to develop software for export since 1970, but production has been hindered by acute shortages of computer hardware. Nonetheless, software exports have more than tripled since the late 1970s and are presently valued at about \$20 million a year. New Delhi plans to boost this level to \$300 million a year by 1990. [REDACTED]

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Increased domestic computer production and the expected influx of advanced western-origin systems in the coming years are expected to provide the equipment necessary for this expansion. By easing onerous production restrictions, New Delhi hopes to increase computer production from approximately 5,000 units a year now to 100,000 units annually by the 1990s. The government has also lowered duties and eased regulations governing computer imports for companies involved in the software trade. And it has decided to encourage exports further by allowing private firms to set up their own export processing zones for software products. [REDACTED]

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Indian software capabilities have attracted considerable foreign interest. Several US companies--including Burroughs, Tandy, and Data [REDACTED]

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General--have already set up operations using Indians to write computer software. According to press reports, Texas Instruments, Hewlett-Packard, and ITT are investigating a system to link Indian software specialists via satellite to computers in the US. India and Norway recently agreed to set up the Indo-Norwegian Software Development and Export Company to produce jointly software for the Indian, Norwegian and international markets. Indian software promotion will almost certainly generate even greater interest in the Soviet Union, where software capabilities are known to be weak. For some time the Soviets have used Indians to develop and convert western origin software for their computers, many of which are direct copies of western machines.

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Central Intelligence Agency



Washington, D. C. 20505

DIRECTORATE OF INTELLIGENCE

29 May 1985

Economic Policy Themes: Technology and Productivity

Rajiv Gandhi's interest in technology and productivity has revived efforts to ease government restrictions on private production and investment. His liberalization moves, although limited, are very significant by Indian standards. Gandhi still intends for the government to retain control of the economy, but he believes that less bureaucratic meddling and more competition in the private sector will spur modernization. limit corruption, and ease strains on the government budget.

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Gandhi inherited policies that protect most Indian businessmen from foreign and domestic competition. Since becoming Prime Minister, he has:

- Permitted manufacturers in several industries to establish or expand capacity and vary their product mix without seeking government permission.
- Relaxed antimonopoly legislation.
- Lowered personal and corporate tax rates.
- Encouraged imports of high technology.
- Pushed the bureaucracy to expedite decisions that affect business.

The electronics industry is a major beneficiary of these concessions. Gandhi is interested in computers and is convinced that India must not be left behind in the scientific revolution in microelectronics.

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The new economic approach is a pragmatic effort to improve sluggish growth rates and increase returns to past investment in Indian industry--not an ideological shift. The basic structure of government controls remains:

- Gandhi continues to stress self-reliance even while highlighting India's need for foreign help with high technology.

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Gandhi's initial moves have fueled an unprecedented atmosphere of optimism among corporate leaders, who are now actively planning new investments and seeking increased cooperation with US and other Western

firms. They hope to build on an economy that has been buoyant recently as a result of increased foodgrain and crude oil production and financial support from the International Monetary Fund. [REDACTED]

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Economic policy is still evolving, and Gandhi's resolve to create a more competitive environment is yet to be tested. Protests from businessmen who must adjust to reduced protection are just beginning to mount, and criticism that Gandhi is slighting the poor in favoring India's middle class is emerging as a significant political issue:

-- One senior official recently told US Embassy officers that the government has 18 to 24 months to demonstrate its effectiveness. [REDACTED]

Gandhi's policy reforms, in our view, do not assure faster overall growth. His decontrol moves directly affect only a small share of the Indian economy. Even if liberalization is extended substantially, the potential benefits can be realized only if the chronic problem of electricity shortages becomes less severe and if agricultural output increases sufficiently to sustain domestic demand for manufactured goods:

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-- Perhaps most important, forthcoming balance-of-payments strains may block India's ability to import goods needed to modernize and increase production. [REDACTED]

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Washington, D. C. 205

DIRECTORATE OF INTELLIGENCE

29 May 1985

International Financial Risks

India's international financial position, which is now comfortable, will probably begin to deteriorate within the next two years, and strains will increase for at least the remainder of the decade. Wary of a Latin American-type debt crisis, New Delhi will probably respond by retreating from liberalized economic policies and by slowing domestic growth. Under such circumstances, the United States would, in our view, come under increasing fire for its policies toward multilateral lending institutions.

Some deterioration in India's financial situation seems inevitable:

- India must soon begin repaying International Monetary Fund loans that provided financial support during the past five years.
- Its petroleum import bill will probably increase, now that domestic oil production has peaked. Geological prospects for further discoveries are poor.
- Despite favorable financial terms offered by the Soviet Union, payments for military imports will rise sharply.
- Debt service payments to commercial lenders will also increase, while 30 years of borrowing on concessional terms have left a legacy of substantial repayment obligations to aid donors.
- In addition, cuts in India's share of multilateral loans, particularly from the International Development Association, presage a hardening of overall borrowing terms and probably a drop in concessional aid receipts.

The recent liberalization of economic policies is intended, in part, to improve the quality of Indian manufactured goods and make them more competitive in world markets. Prospects for the rapid growth in the volume of exports needed to avoid balance-of-payments strains are poor, however, because the pull of the large and more profitable domestic market remains strong:

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- Past liberalization efforts have, in fact, only increased the demand for imported capital goods without stimulating exports significantly.

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If balance-of-payments strains become severe, as now seems somewhat more likely than not, the most likely policy response is renewed curbs on imports and import-intensive industries. Gandhi has not yet commented on international financial issues, but Indian policy is traditionally conservative:

- Wary of a debt trap, his economic advisers are reluctant to risk a substantial increase in commercial borrowing to finance imports.
- Although eager to benefit from foreign technology, they are not seeking investment funds as relief from balance-of-payments strains.

The United States would probably be the scapegoat for any slowdown in policy liberalization that curtails potential economic growth:

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- In the past, Indian officials have perceived an anti-India bias in US policies that curtail New Delhi's borrowing from multilateral lending institutions.
- Increased military payments--if they become widely known in India--would probably be blamed on the need to counter US support for Pakistan.
- Western protectionism, already an issue for a few commodities, would be cited as an explanation for failure to increase exports.

Conversely, ties with the Soviet Union will appear especially valuable when financial strains mount, because payments to Moscow are made through a bilateral clearing account, rather than in hard currency.

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